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CHARLES ELMORE

IN THE

Supreme Court of the United States.

OCTOBER TERM, 1936.

No. 500.

GUY S. MARTIN,
Petitioner,

v.

NATIONAL SURETY COMPANY, a Corporation, et al.,
Respondents.

RESPONDENTS' BRIEF AND ARGUMENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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I.

STATEMENT.

Most of the facts are sufficiently summarized in the opinion of the Circuit Court of Appeals found at pages 154-162 of the record. The findings of fact of the trial court following the hearing on the merits of the issues joined by the amended bill of complaint and the amended answer of defendants Guy S. Martin and A. C. Tobin, which are found in the record at pages 26-28, and the

findings of facts of the trial court following the last hearing in the cause at which the various claims of laborers and materialmen and of the petitioner Martin, were heard and adjudicated, appearing in the record at pages 43-49, will also be found enlightening.

We add the following additional facts. Petitioner Guy S. Martin was an agent with authority to execute surety bonds on behalf of the National Surety Company (plaintiff below) in the early part of 1932, when the matter arose of executing a construction bond for A. C. Tobin & Company, a construction company engaged in the erection of federal public works. Martin had been having quite a bit of dealings with A. C. Tobin of said construction company (R. 105), which were described by Tobin as follows:

> " 'My arrangement with Mr. Martin started back at the beginning of the Havana Post Office job. At that time I was the low bidder and Mr. Martin wrote the bond; my financial standing was weak. While there was nothing in writing, it was agreed that if I needed funds at any time, I could get a lift from Mr. Martin. In return for that, at the completion of the various jobs, the profits were to be divided on a 50-50 basis. That arrangement commenced on the Havana job and carried right on through the Carlinville job' " (R. 138).

Martin's prior dealings with Tobin were in his individual capacity and not as representative of the National Surety Company. The vice-president of the National Surety Company, upon hearing that his company was considering executing Tobin's bond on the Carlinville Post Office job, which is involved in this litigation, expressly instructed petitioner Martin not to execute such bond on behalf of the National Surety Company, but Martin violated those instructions and bound and obligated the Na-

tional Surety Company on the bond in spite of the vice-president's instructions not to do so (R. 80).

In conjunction with this matter, Martin, as agent for the Surety Company, had the contractor, Tobin, execute a written application for such surety bond, wherein it was expressly warranted **"that the applicant (Tobin) has not assigned and would not assign his payment on this contract or any part thereof"** to anyone (other than the National Surety Company) (R. 89). Said application also contained an assignment by the contractor to the Surety Company, of all the deferred payments as well as the retained percentages (R. 91).

In the fall of 1932 the contractor was getting into financial difficulties and defaulted in making payment of the accruing labor and material bills (R. 84, 85). In December, 1932, the Surety Company demanded joint control of the balance of the funds due from the Government (R. 107). The date of this demand was December 20, 1932 (R. 83). The contractor, Tobin, advised the Surety Company that he wanted to see his attorney about executing the power of attorney given to him by the Surety Company for that purpose. However, instead of executing and returning the power of attorney, Tobin took it to Martin (R. 108). The next day, December 21, 1932, Martin procured a new power of attorney, executed by Tobin to Martin (R. 99, 101). Martin also prepared a letter to the Treasury Department, which Tobin likewise signed, directing that all of Tobin's checks be forwarded to petitioner, Guy S. Martin (Exhibit H, R. 117). On December 28, 1932, Martin forwarded the power of attorney and the letter written by Tobin to the Treasury Department (R. 117).

Between December 20, 1932, and February 6, 1933, when Martin actually collected the money from the Government, various officials of the National Surety Company had conferences with Martin concerning the difficulties that had

arisen by virtue of the contractor's nonpayment of labor and material bills (R. 81-83). Martin at all times concealed the fact that he had said power of attorney and that he claimed to have money due him on account of loans made to the contractor, Tobin (R. 82, 83). The contractor, Tobin, like Mr. Martin, also actively misrepresented and concealed from the Surety Company the true facts with respect to having executed a power of attorney in favor of Martin and with respect to the fact, if it be a fact, that Tobin owed Martin any money (R. 86, 87, 108).

While Martin's explanations of the purposes of the power of attorney, which was executed in his favor, are not without conflict, his first statement under oath about the matter, is as follows:

> "When he (Tobin) gave me the power of attorney he said **there were going to be some bills to pay and he wanted me to handle these funds**" (R. 99).

The time specified in the Government contract for the completion of all work on this particular job was January 18, 1933, and a penalty of thirty-five dollars ($35.00) per day was provided for failure to complete the building on time (R. 79). It was not until February 6, 1933, that petitioner Martin collected the money in question from Washington (R. 96) as a result of the hurried trip which he made in secrecy even from Tobin's attorneys (R. 86, 87, 101, 108), who appeared in this case as Martin's attorneys about ten days later (R. 16). The Circuit Court of Appeals found that the moneys which Martin collected and which are involved in this case are payments which were made to him as attorney in fact for the contractor, after completion of the contract. That Court further found that Martin had full knowledge of all of the facts in connection with this entire matter (R. 161).

II.

ARGUMENT.

Not only do the rules of this Honorable Court provide: "A review on writ of certiorari is not a matter of right, but of sound judicial discretion, and will be granted only when there are special and important reasons therefor" (No. 38 of the Revised Rules of the Supreme Court of the United States). But also in the case of **Furness, Withy & Company v. Yang-Tsze Insurance Association, Ltd., et al., 242 U. S. 430**, this Court directed the attention of the members of the bar to the fact that a duty rests not only upon counsel for petitioner, but also upon counsel for respondent, to give this Court all information available that will assist it in determining the appropriateness of the relief prayed for to the facts of the case at hand. We address ourselves to the discharge of that duty.

Petitioner suggests three reasons why this Court should allow a writ of certiorari in this case (Petition for Writ of Certiorari, page 8). The third of these reasons, to wit, that the Circuit Court of Appeals herein has decided the case in a way probably in conflict with applicable decisions of this Court, has not the slightest semblance of merit. See **Henningsen v. U. S. Fidelity & Guaranty Co., 208 U. S. 404; Prairie State Bank v. United States, 164 U. S. 227,** and **American Surety Company v. Westinghouse Manufacturing Co., 396 U. S. 133.**

The second reason suggested is that an important federal question has been decided by the Circuit Court of Appeals, which should be settled by this Court. Such suggestion is not persuasive when we consider the time that this Court has already devoted to a consideration of

the equitable rights of sureties and of laborers and materialmen arising under the Hurd Law (see cases last cited, supra). In the Henningsen case this Court held that the surety on the contractor's bond who had paid the claims of laborers and materialmen became thereby subrogated to an equity in the funds due from the Government under the contract. Such equitable rights were held to be superior to the rights of a bank holding an assignment from the contractor to secure moneys loaned. The opinion in that case states:

> "Whatever equity, if any, the bank had to the fund in question arose solely by reason of the loans it made to Henningsen. Henningsen's surety was, upon elementary principles, entitled to assert the equitable doctrine of subrogation, but it is equally clear that the bank was not, for it was a mere volunteer, and under no legal obligation to loan its money."

Judge Denison of the Sixth Circuit, in the case of **Belknap Hardware and Manufacturing Company et al. v. Ohio River Contract Company et al., 271 Fed. 144,** has made the following careful analysis of the basis of this Court's decision in the Henningen case, to wit:

> "It may fairly be assumed, we think, that there was some general recognition of this moral or ethical duty resting upon the United States, and that this led to the passage of the Bonding Act of 1894. The policy of the act may be thought of in two ways. It may have been the congressional intent to substitute this statutory bond, as a protection to laborers and materialmen, in place of the rather vague obligation, which had been to some degree assumed by the United States, to look after their interests, in which case this obligation was eliminated, and after the statute, there

was no such duty resting on the United States and no such right to protection remaining in the laborers. It may have been the congressional intent to give to these claimants, by this bond, an additional protection, which would become the ordinary and primary one, and usually would be sufficient, and to do this without diminishing the obligation of the Government to see that these claims were paid, as far as that result could be accomplished by the funds which it retained. In that event the equitable priority of such claimants in the fund, if such priority there had been, would remain and could be enforced in the appropriate cases either directly or by subrogation.

"It is not necessary to consider which of these views would seem the better one, if the question were open. We think it has been foreclosed by the decision of the Supreme Court in Henningsen v. U. S., 208 U. S. 404, 28 Sup. Ct. 389, 52 L. Ed. 547."

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"The surety's claim of priority in the fund was sustained, and this was done on the stated theory of subrogation. **Since there cannot be the transfer of a right by subrogation, unless there is a right to be transferred, we think the necessary effect of the decision is to hold that the laborers and materialmen, in spite of or in addition to the giving of the bond, had an original and continuing equitable priority in the fund**, and that it was this right to which the surety was subrogated. This is not stated in the opinion in very express terms, but it had been pressed upon the Court (208 U. S. 407, 408, 28 Sup. Ct. 389, 52 L. Ed. 547) that there could be no such subrogation without such a right, and that there was no such right. On page 410, of 208 U. S., on page 391 of 28 Sup. Ct. (52 L. Ed. 547), the Court refers to and assumes that the Government, after the bond was given, was still charged

> with 'equitable obligations to see that the laborers and supply men were paid.' We are constrained to think that the decision necessarily rests upon the existence of this right, as one entitling these claimants to priority in payment out of the fund, and therefore as entitling the surety, as their equitable assignee by subrogation, to the same priority."

Not only has this Honorable Court thus recognized the existence of the equitable lien of laborers and materialmen under the Hurd Law by its decision in the Henningsen case, supra, but it has reaffirmed its views on this matter in the following excerpt from the opinion from Mr. Justice Cardozo, speaking for this Court in the case of **American Surety Company v. Westinghouse etc.**, supra:

> "Through the bond and the statute a new relation has been established with a new set of equities not subject to destruction at the pleasure of the principal (contractor). The integrity of that relation is in the keeping of the law.
>
> "We have on occasion to consider to what extent the creditors of the bankrupt not covered by the bond are affected by **the equities of creditors so covered** or by those of the petitioner, with the result that their claims are to be held subordinate thereto. Cf. Prairie State Natl. Bank v. U. S., 164 U. S. 227, 41 L. Ed. 412; Henningsen v. U. S. F. & G. Co., 208 U. S. 404, 52 L. Ed. 547."

The only remaining reason relied on for the allowance of the writ is that the opinion and decision of the Circuit Court of Appeals in the instant case creates a conflict with decisions of other Circuit Courts of Appeal on the same matter. Petitioner's able counsel, after their usual exhaustive search of the authorities, have cited four cases

upon which they predicate their suggestion that the decision in the instant case is in conflict "with decisions of other Circuit Courts of Appeal in the same matter." **Not a single one of those cases involves a federal public works.** It appears from the cases relied on by petitioner that they arose on public works under the various state statutes.

The case of **Fidelity & Deposit Company v. Union State Bank, 21 Fed. (2d) 102,** relied on by petitioner, was decided by the **District Court** in Minnesota. The basis of the decision is set forth in the opinion as follows:

> "It is equally well settled, **at least in the State of Minnesota,** that where payments are made to a public contractor unconditionally, under a contract such as is involved here, he can use the money so paid in any way he desires, and the payment is not subject to any equity. **Jefferson v. Church of St. Matthew,** 41 Minn. 392, 43 N. W. 74; Miller v. Shepard, 50 Minn. 268, 52 N. W. 894; Board of Commrs. of Redwood County v. Citizens' Bank, 67 Minn. 236, 69 N. W. 912; American Bridge Co. v. Honstain, 113 Minn. 16, 128 N. W. 1014; Villaume Box & Lumber Co. v. Condon, 146 Minn. 156, 178 N. W. 492; Standard Oil Co. v. Day, 161 Minn. 281, 201 N. W. 410, 41 A. L. R. 1291."

The case of **Maryland Casualty Company v. Board of Water Commissioners, 66 Fed. (2d) 730,** relied on by petitioner, relates to a public works of the City of Dunkirk, New York. It does not involve a federal public works or any question of the equitable rights that may arise under the federal statutes. The basis of the decision in that case appears to have been that when the bank collected the money in question from the municipality on its assignment from the contractor, "it was twenty days before a

default was declared by the Board. The Bank had no notice of the prior **unrecorded assignment** to the surety, and therefore we see no basis for asserting that the surety had a prior equity in payments due to Loyd under the terms of the contract." From this statement of the Court, it may be assumed that some provision is made under the statutes of the State of New York for the **recording** of assignments such as the surety predicated its rights on in that case; and the surety's **failure to record its assignment** was the basis of its loss of right.

The two remaining cases relied on by petitioner, to wit, **Kane et al. v. First National Bank of El Paso, Tex., 56 Fed. (2d) 534,** and **Third National Bank v. Detroit Fidelity & Surety Co., 65 Fed. (2d) 548,** were each decided by Judge Sibley of the Fifth Circuit. The former involved a contract with a school district under the state laws of Texas and the latter involved a contract with the State Highway Department of Florida. In the Kane case progress payments were **actually paid over to the contractor** and by him deposited in the bank to whom he owed money, **long prior to the completion of the contract** and prior to any default by the contractor; whereas, **in the instant case the funds in question are moneys that remained in the Government's hands after the completion of the contract.** The contractor, Tobin, was then insolvent, and the unpaid claims of laborers and materialmen on the job in question totalled about twenty-five thousand dollars ($25,000.00) (R. 50-53). The trial court and the Circuit Court of Appeals held that Martin had knowledge of all of the facts (R. 161).

In the Third National Bank case, supra, relied on by

petitioner, the Court expressly found the **surety company not only knew of the bank's assignment, but acknowledged it, and was therefore estopped to assert its prior lien (65 Fed. [2d], l. c. 550).**

Admittedly there are statements in Judge Sibley's opinions in the two cases last cited from the Fifth Circuit, which tend to support petitioner's contention that the lien of the surety company is limited to the retained percentage. However, in the most recent case in which the United States Circuit Court of Appeals for the Fifth Circuit has considered the question of equitable liens in connection with a federal public work, the majority opinion (from which Judge Sibley dissented) states:

> "It appears from decisions referred to below that the Government's observance of that duty in practical and effective ways, was the precursor of judicial recognition of an enforcible, equity right of unpaid furnishers of labor or materials for that work in or to a part of the contract price thereof remaining in the possession of the Government after the completion of that work by the contractor" (American Surety Company v. Westinghouse Electric Manufacturing Co., 75 Fed. [2d] 377, affirmed by this Court in 296 U. S. 133).

It therefore appears that the last decision from the Fifth Circuit is in accord with the decision in the instant case.

In conclusion, respondents respectfully urge that the disposition made of this case by the District Court and affirmed by the Circuit Court of Appeals is in accordance with sound reason and the justice of the case.

We ask, therefore, that the petition for a writ of certiorari be denied.

Respectfully submitted,

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